

To: Carl Pascarella  
cc. Victor Dahir  
From: Andrzej Lubowski  
Re: Battle for Market Share  
Date: July 24, 1997

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What follows is an updated and abbreviated version of my June 20<sup>th</sup> memo to Bill, Michael, Vic, Paul and Randy. Its objective is to share with you my thoughts regarding our current battle for market share with MasterCard.

I strongly believe that our overall objective is to protect/grow market share vs MasterCard. *The need to arrest the downward trend in share-of-mail, important as it may be, is not the end but the means.*

I would argue that both political as well as business risks associated with buying mail far outweigh very uncertain and definitely very costly and temporary rewards. I believe that some other weapons in our arsenal can deliver faster and more sustainable benefits, with higher and more predictable returns on investment. Let me spell out my concerns with our focus on buying mail.

#### **Political implications**

Political risks are pretty obvious. Should we decide to buy mail to protect market share, in order to make a difference we would have to allocate available resources to a very limited number of large, very aggressive Members. The rest of Membership would end up subsidizing efforts which would unavoidably hurt their businesses. The political fallout is difficult to dimension. Even if we were able to control it this time, what would stop this practice in the future?

#### **Likely cannibalization**

Given our current share of cards, the probability of Visa to Visa conversion as a result of mail solicitation is high. The most powerful incentive to switch from one card to another is to lower initial rate or eliminate a fee. Therefore, our efforts will support teaser-to-teaser migration and fee erosion, two phenomena which have already driven down sharply the profitability of our Members.

#### **Potential for deteriorating the overall credit quality**

Overwhelming majority of credit-worthy individuals already carry credit card(s). Increasing saturation in the already saturated market carries a risk of: a) increasing credit exposure of current cardholders or/and b) soliciting from a less credit worthy population, both of which carry obvious risks. In the first quarter of 1997, more than two-thirds of total losses of banking industry came from credit cards.

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GOVERNMENT  
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Francine Schall

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#### **Uncertain activation and usage**

It will not do us any good if incremental cards are not used or used infrequently. When a customer accepts an offer to add another card to his wallet - why not, if it costs nothing - (rather than replacing a current card) he or she may not use it or use it sporadically. If that happens we will never recover our costs.

#### **High probability of public/regulatory criticism**

Spending significant funds on supporting mail solicitation will expose us to public criticism for fueling the avalanche of credit card solicitation.

#### **Temporary nature of potential victory**

And finally, the key source of my discomfort with using mail purchase as primary weapon against MasterCard is the temporary nature of potential victories. Assuming that a MasterCard is converted to Visa, this new card with our logo is as vulnerable to a switch as the one it replaced.

At the end of the game we and MasterCard would have spent millions of our Members' money in what looks like a zero-sum game. It would not, however, be a zero-sum game. In fact it would cost the industry dearly (lower finance charges, less fees, in all likelihood more charge-offs, not to mention funds spent by us and MC in the process).

The alternative weapon to protect/grow our market share vis-a-vis MasterCard is to supplement our Merchant Relations/Market Acceptance efforts to expand acceptance and usage, with strong, aggressive focus on buying debit decisions and intensifying efforts to activate and stimulate card utilization.

Debit card is significantly less vulnerable to switch. And given its infant stage, debit is also more likely to generate incremental volume.

We should review debit programs of top 100 (or more) financial institutions. To those who don't have debit offering we should try to sell our brand. For those who already chosen us, let's offer an aggressive activation and utilization support. I believe that in the short term there is nothing as productive and supportive to our market share protection and growth as debit efforts.

I am attaching a set of scenarios which illustrate the impact of fast growth of debit on overall Visa share vs MasterCard. Given our current advantage in debit volume (85% Visa vs 15% MC share), maintaining a high growth of debit (without neglecting other categories) is the single most important way to protect/grow our market share. Its impact is so powerful that as long as we grow debit volume in the 40%+ territory annually, we could even afford the

luxury of losing a bit of market share in all key product categories and still increase our overall market share.

It sounds counter-intuitive, but it is true. The reason why it is possible is the significant advantage we have on the debit side, and that debit share of our total business is growing fast. For example, if we were to grow our credit category at 12% a year vs 14% for MasterCard, grow commercial card volume at 30% vs 35% for MC, but grow debit at 45% vs MasterCards' 50%, (in other words, surrendering share in all categories) our overall market share would go up from 66.2% today to 66.6% in 1999 and 68.1% in 2002. If we were to keep pace with MasterCard and grow credit by 13%, commercial by 30% and debit by 50% annually, in five years we would exceed your goal of 70% market share vs MasterCard (71.3%). That's why it is so important from the overall market share point of view not to allow MasterCard shrink the gap separating us today in debit arena. We have to do all we can, as soon as possible, to keep the distance.

One more comment: we can not devote all our energies to fight MasterCard (and our Members will not support us in this fight) at the price of neglecting our Members' true rivals: American Express or Dean Witter, and emerging rivals such as Microsoft and FDC. We can win this battle with MasterCard, but unless we improve our products and find a better way to leverage our brand we may not be able to prevail in the war.

A decade ago, Walter Wriston, speaking about new entrants into banking industry taking away banks' customers, as bankers were debating among themselves, said:

*"We have been a little like those people in Gulliver's Travel who fought a war over whether the soft-boiled egg should be opened from the small end or the large end. While we are fighting our war, somebody is stealing the chicken."*

*In summary, I believe that "Buy Mail" as a key weapon to protect market share has a very unpredictable/questionable pay-off with numerous significant risks; at best provides only a temporary relief (and like morphine carries a high risk of creating an addict).*

Given your previous conversation with the Board, and their position, I am submitting for your consideration the following adjustment:

Reiterate our mission: *Support Members' Profitability and Preeminence*

After careful consideration, Visa management asks the Board to reexamine our previous request for defensive resources. While spending \$50MM to fight MasterCard buying of mail-solicitation would help Visa protect its market share,

it is highly questionable whether and how it would support Members' profitability and preeminence.

We strongly believe that MasterCard aggressive stand:

- fuels two trends which hurt the industry's profitability:  
erosion of fees and teaser-to-teaser migration;
- carries a risk of exasperating credit quality problems;
- is ethically questionable (all Membership is supporting selected few);
- is likely to damage the industry image in the eyes of the public, regulators and legislators

We don't believe that such a practice is healthy for the industry. Recognizing that the mid- and long-term threats are coming from American Express and new players likely to encroach on the banking industry's territory we recommend to focus our attention and resources on:

- opening new markets;
- promoting card activation and usage;
- enhancing existing and developing new products;
- promoting new technologies.

As I said before, I believe that an alternative is a bloody spending spree funded by the industry, which will sooner or later remind us about it. Should we decide to accept MasterCard rules of game, results, even under best case scenario, will not show in the second, third and probably fourth quarter of this year. I would submit that we may be better off demonstrating statesmanship, climate setting for drop in our market share and requesting authorization of spending significant resources for other purposes. (debit, e-Pay, chip terminalization being some candidates).